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Central Intelligence Agency

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Washington, D. C. 20505

## DIRECTORATE OF INTELLIGENCE

6 May 1985

Western Competition for Soviet Contracts**Summary**

Soviet orders for machinery and equipment in 1984 reached their lowest level in over a decade due to Moscow's disappointment with the overall benefits of previously imported equipment and their desire to reduce dependence in the wake of Western sanctions. Nevertheless, the USSR continues to look Westward for select technologies, often integrated in complete plant purchases, to address key bottlenecks and technological lags. [REDACTED]

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The Soviets are currently involved in intensive project negotiations with Western firms which are likely to result in sizable contracts in the near future. Judging from ongoing negotiations and our assessment of Soviet domestic shortfalls, technology and equipment purchases will be concentrated during the 12th FYP in:

- o Oil and gasfield equipment to stem the falling oil production, increase offshore exploration, and accelerate natural gas production.
- o Chemical equipment to boost Soviet fertilizer and synthetic fiber production.
- o Agricultural production and food processing equipment to support consumer welfare goals. [REDACTED]

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Once import priorities are set and allowances made for broader political considerations, the typical Soviet purchasing strategy is to obtain the needed technology and equipment on the best terms possible.

- o Moscow, for its part, has paid lip service to Western demands for preferential treatment such as redressing trade imbalances.
- o While Moscow used the lure of major contracts to keep West Europeans from adopting US proposals to limit energy and advanced technology trade, contracts ultimately went to those firms offering the best commercial terms.

This memorandum was written by the Economic Performance Division, SOVA with contributions from Strategic Policy Division, SOVA, West European Division, EURA and Northeast Asia Division, OEA. Comments and queries are welcome and may be directed to Chief, Economic Performance Division [REDACTED]

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West European firms--who generally have the necessary technology, offer attractive financing, and have longstanding ties with Soviet buyers--are likely to continue to get the lion's share of Soviet business. While Japanese technology is highly competitive, Japanese unwillingness to agree to Soviet countertrade demands will limit their equipment sales. [REDACTED]

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Recently the USSR has tantalized US businessmen with the prospects of lucrative deals and have toned down allegations that US suppliers are unreliable. This marks a sharp reversal from recent years when US-imposed sanctions and export controls led Moscow to consciously and openly avoid US businesses. Improved US-Soviet relations coupled with some movement on the sanctity issues could open the door for increased US sales especially where the United States has a clearcut technological advantage--indeed some small deals have already been concluded--but events over the last ten years have eroded the competitive position of US firms and thus it is not likely that the United States will regain the position in Soviet trade it once had. [REDACTED]

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[Redacted]

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### Current Trade Position

The USSR's surplus on hard currency trade fell only slightly in 1984 to \$4.3 billion in spite of record imports of grain and a decline in the value of hard currency exports of arms to the less developed countries (LDCs). Imports of machinery and equipment and of pipe fell substantially because of the completion of deliveries for the Siberia-to-Western Europe gas pipeline. Purchases of non-grain agricultural products also declined. The value of oil exports increased slightly as a 5.5 percent rise in volume more than offset a 3 percent decline in average prices.

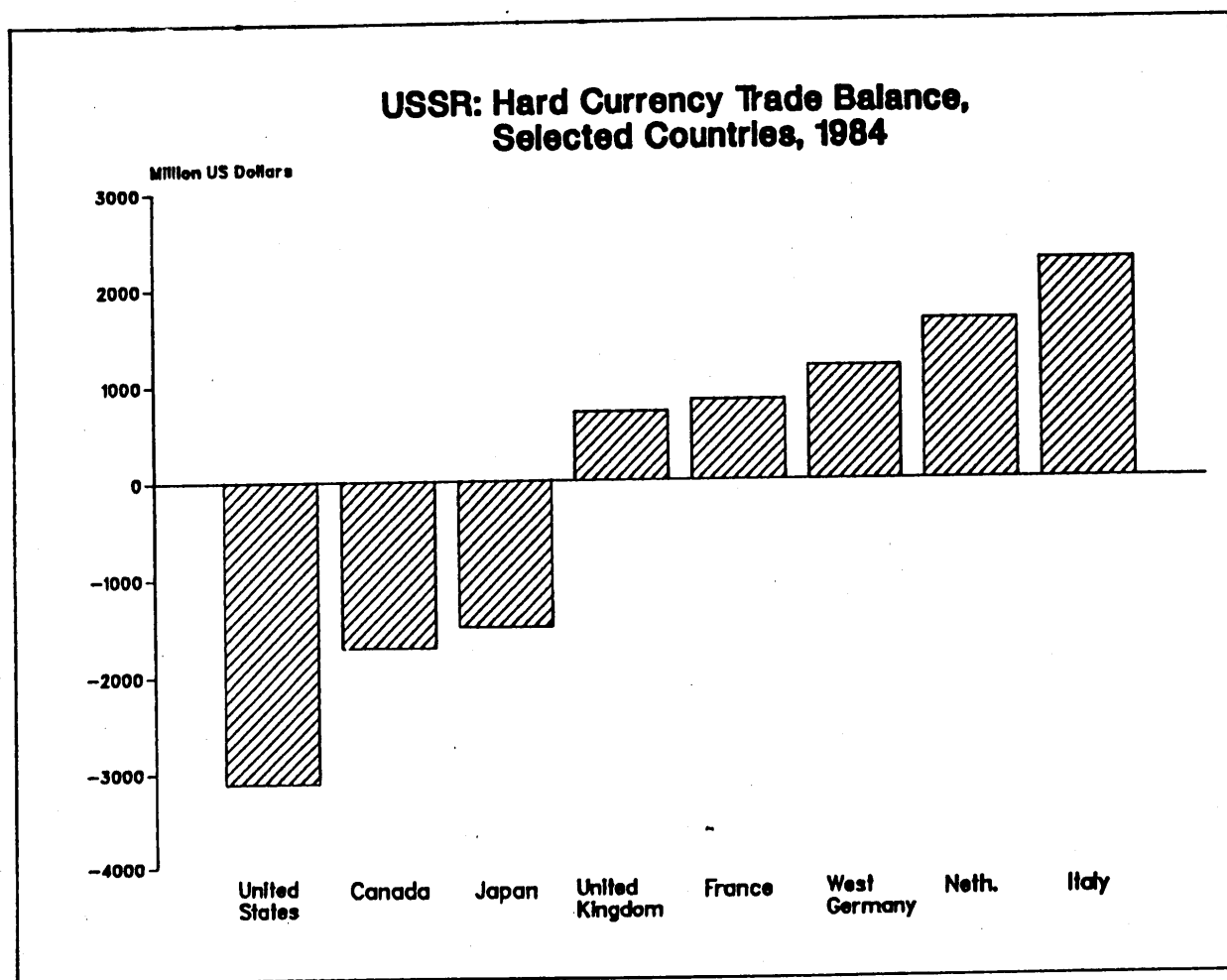
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The USSR continued to run trade surpluses with nearly all of its West European partners, the largest being with Italy (\$2.3 billion), West German (\$1.4 billion), and the Netherlands (\$1.6 billion) (see figure 1). Moreover, most of the USSR's hard currency credits continued to be provided by West European countries. Moscow also ran surpluses with most LDCs. The countries with which the Soviets ran deficits were--for the most part--the ones from which they imported sizable amounts of agricultural products (the United States, Australia, Canada, Argentina, and Brazil). The USSR has used the bulk of its excess earnings from energy exports to Western Europe to pay for imports from those countries with which it is in deficit.

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About 83 percent of Soviet exports to the West European countries consist of oil and oil products and natural gas.

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Nearly all of the USSR's imports from these countries, on the other hand, consist of machinery and equipment and other manufactures and semi-manufactures. Real imports of machinery and equipment declined an estimated 40 percent in 1977-81, rose more than 50 percent with deliveries for the new gas export pipeline in 1982-83, and declined roughly 15 percent in 1984.

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West European countries--most of which are facing high unemployment and economic stagnation--have been pressing Moscow to step up its purchases but to little avail. But because these countries must import oil and gas, they have little leverage in forcing Moscow's hand. The other possible energy suppliers are not apt to increase imports from Western Europe either. The USSR, for its part, will continue to welcome these surpluses since they can be used to help pay for purchases of grain and other agricultural goods from countries such as the US that are unlikely to try to narrow their surpluses by greatly increasing imports from the Soviet Union.

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#### Outlook for Hard Currency Imports

Beyond 1985, our projections of Soviet oil production and availability for export spell trouble for the Soviet hard currency payments position. Unless Moscow revises its cautious borrowing policy, constraints on exporting oil for hard currency could well force the USSR to reduce the volume of imports from hard currency countries at least through 1990. But our analysis,

[REDACTED]

under the worst case scenario for energy exports, imports from the West could drop by as much as 20 percent over the remainder of the decade.<sup>1</sup> Our best guess is that Moscow will face a less severe drop in energy exports and will step up borrowing somewhat to keep import volumes at roughly current levels.

The extent to which the 1982 Food Program succeeds in making the USSR more self-sufficient in agricultural production will largely determine how much the Soviets can spend on nonagricultural goods. With hard currency resources limited Moscow will have to choose between competing domestic requirements.

- o As a first priority, we believe the USSR will try to import sufficient quantities of grain and feedstuffs to keep the livestock program on track.
- o Its second objective probably will be the industrial materials needed to prevent production bottlenecks, and the equipment and technology to help develop and exploit energy sources.
- o Its third priority might well be equipment and technology for other key areas. [REDACTED]

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While Moscow no doubt expects much of the increase in imports of machinery and equipment to come from Eastern Europe, which now provides about two-thirds of such imports, it is likely

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to continue to import sizable quantities from hard currency countries. These purchases totaled \$7 billion in 1983. The Soviets will need Western machinery and equipment for the energy industries, agricultural and food processing industries, machine tool production, construction and transportation projects, process control and other electronics industries, and chemical production. If unable to acquire Western machinery and technology, the Soviets could go it alone, but would sustain appreciable losses in quality, reliability, and productivity in some sectors. [REDACTED]

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#### Status of Project Negotiations

Current Soviet project negotiations with Western firms indicate that Soviet purchases of machinery and equipment for the next five-year plan will focus heavily on energy-related equipment and technology. Of the more than \$20 billion in potential sales to the USSR, over 70 percent are for the energy sector. [REDACTED]

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The USSR has expressed the most interest in Western participation in the development of major oil and gas fields. Initial contracts for Tenghiz and Astrakhan II have already been signed and additional contracts for this project as well as Karachaganak are expected to be awarded soon. Other projects such as the Barents Sea Petroleum Development project and the

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Irkutsk and North Star liquified natural gas projects are in early stages of discussion but have the potential for generating billions of dollars in orders by the end of the century. [ ]

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There has also been a resurgence of Soviet interest in purchases of Western technology and equipment for the chemical sector, particularly in the form of turnkey projects. We expect that purchases for the 12th Five Year Plan could exceed \$2 billion. The USSR is also negotiating projects in the metallurgy, automotive, electronics, and machine tool sectors which are designed to selectively improve the quality and assortment of output in those sectors. [ ]

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Finally, the adoption of the Food Program in 1982 has resulted in increased interest in Western equipment and technology in the agricultural and food processing sectors. Although most of Moscow's increased imports are likely to come from Eastern Europe, purchases from Western firms of selective types of equipment are likely to expand. Because most of the projects will be on a much smaller scale than those projects being negotiated in the energy and heavy industry sectors--under \$50 million--the relative share of these purchases in total Soviet orders will remain small. [ ]

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#### Competing Western Interests

The major contenders for projects likely to be signed in the near future are German, French, Italian, and Japanese firms. The West Germans, as in the past, will probably capture the lion's

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share of the contracts for projects included in the next five year plan.

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The French are also likely to win sizable contracts with the Soviets. It was announced in early April, for example, that contracts for the gas processing plant at Astrakhan and the gas desulphurization unit at Tenghiz, valued at \$400 million, would be signed soon. Meanwhile, the Italians have already signed contracts worth about \$300 million this year and negotiations for several other contracts worth over \$2 billion are reportedly approaching conclusion.

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The West Europeans currently have an edge over other competitors in obtaining lucrative Soviet orders. Their governments have long pursued a policy of expanding trade with the USSR. Government-backed credits at attractive interest rates are frequently offered and COCOM restrictions are generally less rigidly interpreted than in the US. In contrast, US policy since the mid-1970s and particularly the 1980 and 1982 sanctions have driven the USSR to find alternatives to US grain and machinery and equipment. US firms received only 4 percent of Soviet equipment orders last year compared to a 25 percent share in the early 1970s. Similarly, since the 1980 partial US grain embargo, the US share in total Soviet grain imports has been below 40 percent compared to an average of about 60 percent throughout the

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1970s. The Japanese government has likewise discouraged expanded trade relations but to a lesser extent than the United States.

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The geographic proximity of Europe and Japan to the USSR and their import requirements for most essential raw materials make these countries more amenable to Soviet desires for countertrade arrangements. If, as we expect, the USSR's hard currency position deteriorates, Soviet officials could well increase the efforts to negotiate such arrangements in order to assure their ability to pay for the required technology. Joint Soviet-Japanese development of Siberian resources, in particular, will depend on these types of arrangements. Japanese businessmen, however, do not see sufficient future demand for Siberian resources to justify expanded cooperation on that basis. Thus, many of the projects proposed by the Soviets will proceed slowly at best and the Japanese role in Soviet projects during the 12th Five-Year Plan will likely be limited compared to the European.

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The trade deficits that most West European countries have run with the USSR in recent years may also give these countries an added advantage in their efforts to secure Soviet business, albeit marginal. Despite agreements signed in early 1984 committing the USSR to balance its trade with both France and Italy, equipment orders have not been forthcoming. Indeed, Renault recently cancelled a deal to design and construct an

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automobile plant after the Soviets placed most of the actual equipment orders for this plant with West German firms. In contrast, French pressure may have been partially behind the increased EC--mainly French--grain sales to the USSR during the 1984/85 marketing year (July-June) but subsidized prices and the strong US dollar also made EC grain competitive. Aside from France and Italy, other West European countries have not made much of an issue over the trade imbalances.<sup>2</sup> (see Appendix B for a discussion of selected developed countries' attitudes toward trade with the USSR). [redacted]

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On the other side of the coin, non-European developed countries--US, Canada, Japan and Australia being the most important--generally run sizable trade surpluses with the USSR. Soviet officials have cited these large surpluses as being a hindrance to trade expansion and have pressed firms in these countries to purchase Soviet commodities to at least partially offset Soviet purchases from these firms. In a rare statement of candor, however, Deputy Foreign Trade Minister Zhuravlev stated that the large US trade surplus is not a problem because the USSR could not produce what the United States needed. As long as Moscow requires the products produced by these countries,

<sup>2</sup> In an economic sense, bilaterally balanced trade is not a necessary criteria for a sound trade position. Many countries, however use the issue of bilateral trade deficits to increase exports. The issue takes on a greater urgency when a country, such as France or Italy, runs a chronic trade deficit in its overall trade. [redacted]

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particularly the agricultural commodities supplied by the United States, Canada, and Argentina, these surpluses will remain large. [redacted]

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### Political Considerations

Once import priorities are set and allowances are made for broader political considerations, the USSR's purchasing strategy is to obtain the needed items on the best commercial terms possible. While political considerations have influenced the choice of countries from which firms are requested to bid for Soviet projects (and the choice of firms within those countries), the subsequent choice among competing offers has almost invariably been made by foreign trade functionaries according to select economic criteria.

- o The decision to seek a foreign source for a particular type of plant and equipment is made as part of the overall economic planning process; individual ministerial "wish-lists" are prioritized according to broader production goals and foreign exchange availabilities.
- o Although industrial representatives may provide initial guidance regarding potential suppliers and technical evaluation of foreign bids, the responsibility for commercial negotiations is closely guarded by Ministry of Foreign Trade personnel. [redacted]

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Judging by the emphasis given to select aspects of commercial negotiations, Ministry of Foreign Trade officials are held responsible for demonstrating that they met the technical demands of the industrial ministry--guaranteed delivery and on site performance of imported equipment--at the "best" terms available--lowest purchase price and availability of long-term loans carrying a low nominal rate of interest. (see intext table on politics in Soviet Negotiating Strategies). [REDACTED]

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In Western Europe commercial considerations clearly have been reinforced by Soviet hopes that closer trade ties would complement longstanding political efforts to divide the United States from its allies. These hopes received encouragement in the early 1980s from the failure of US efforts to block West European agreements to purchase large quantities of Soviet natural gas, and from the subsequent willingness of West European governments and corporations to defy US efforts to prevent the sale to the USSR of gas pipeline construction equipment. Ongoing Soviet efforts to circumvent US restrictions on high-technology exports by purchases in Western Europe undoubtedly have this political goal in mind, along with the principal goal of securing denied technology for economic and strategic reasons. [REDACTED]

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In-Text Table

Politics in Soviet Negotiating Strategies

US Embassy officials say that they frequently cannot tell whether commercial concerns--credit terms, interest rates, and reliable delivery--or political factors have more influence on the awarding of contracts. [REDACTED]

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[REDACTED] commercial terms are probably at the heart of Soviet negotiating strategy. Nevertheless, Soviet trade experts inject politics into negotiations both as a ploy to obtain better terms by wearing down negotiators with superfluous demands and as a political message for other governments. The US Embassy in Moscow has noted that in the case of a single import commodity, the Soviets--to obtain better terms--may tell a Japanese exporter that his government supports the United States too much, a German exporter that he should object to the Pershing II, and a Canadian that his country's trade surplus with the USSR is too big. Since the early 1970s Ministry of Foreign Trade leaders have repeatedly argued with US diplomats and businessmen that credit restrictions, US trade legislation, and other US Government actions and policies are barriers to expanded US-Soviet trade.

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[REDACTED]  
[REDACTED] officials of FTOs have become more discriminating in selecting foreign firms since economic sanctions were imposed after the Soviet invasion of

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Afghanistan in 1979; those sanctions resulted in delayed deliveries of equipment and long, fruitless negotiations. According to one Western business journal, a European company with a longstanding relationship with purchasing officials might win a contract even if another competitor, particularly a US firm, offered cheaper terms, reasonable financing, or a better product because the Soviets trusted that European company to make every effort to deliver on time. [REDACTED]

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We note, however, that Soviet trade officials sometimes follow these strategies inconsistently. Some deputy foreign trade ministers, FTO officials, and industrial leaders at times lobby with their superiors for favored US firms with whom they have done considerable business in the past, according to US Embassy commercial officers. At other times, under pressure from the Kremlin, they refuse to deal with those same firms. [REDACTED]

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End In-Text Table

The Soviets sometimes attempt to use their trade ties with Western Europe as a stick rather than a carrot for political purposes. In recent weeks, Soviet officials have indicated that West German trade with the USSR will suffer if West Germany continues to support the United States on the Strategic Defense Initiative and other security issues. The Soviets, however, invoked similar threats during their campaign in 1983 to dissuade West Germany from approving NATO INF deployments, then backed away from implementing them after the Bundestag made its affirmative decision. [REDACTED]

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A number of Soviet statements indicate that calls for improved trade ties with the United States have been motivated by hope of using businessmen to influence US policies, including US positions at the arms control talks in Geneva. [REDACTED]

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[REDACTED] visiting Politburo member Shcherbitskiy claimed in a meeting with US officials in early March that progress in the talks could result in increased bilateral trade. [REDACTED]

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#### LDC Role in Soviet Trade

In general, the USSR runs a sizable surplus in its trade with the less developed countries. Military exports account for almost 70 percent of Soviet exports to the LDCs while imports

consist primarily of agricultural commodities and fuels. Because those countries--mainly in the Middle East and Africa--which actually run large deficits in their trade with the USSR generally have little to offer and are dependent on Moscow for their arms supplies, they are in no position to pressure Moscow into increasing imports from them. [REDACTED]

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In contrast, Soviet trade with LDCs in Latin America and the Far East has usually been in deficit. These countries are the major LDC suppliers of agricultural commodities to the USSR. At the same time, the generally poor quality of Soviet manufactured goods and the distance that separates these countries from the USSR make Soviet exports generally unattractive. The USSR has complained about these imbalances and have gone so far as to state that future purchases from Argentina and Brazil--two of its largest LDC trade partners--depend on efforts by those countries to increase imports from the USSR. Imports from Latin American and the Far East have indeed fallen since their peak in 1981, but largely due to an overall reduction in agricultural imports and falling world commodity prices rather than a deliberate shift in trade away from these regions. [REDACTED]

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These same countries can and, to some extent, do provide Moscow with an alternative to the developed West not only for agricultural products but also some manufactured commodities including machinery and equipment. While imports of manufactures other than textiles remain small--only about \$530 million in

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1983--the Soviets have shown increased interest in such commodities in recent years. Brazilian start-up devices were used on the Siberia-to-Western Europe pipeline, for example, and in late 1982 the USSR reportedly purchased \$100-\$125 million worth of offshore oil equipment from a Singapore firm. It is unlikely, however, that such interest will soon translate into either sizable or sustained purchases, given traditional Soviet preferences for dealing with established firms in the industrialized West, its penchant for advanced technology, and the aftersales services that only the larger firms in the West can provide.

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#### Outlook for the US

Although few of the major contracts currently being negotiated will probably be awarded to US firms, there are increasing opportunities for US firms to expand their sales to the USSR. According to the US embassy in Moscow, since the January Working Group meeting of the Joint Commercial Commission, Soviet foreign trade organizations are no longer withholding bid invitations and a number of US firms have been requested to bid on major projects. A few firms have actually signed contracts recently--though the dollar amounts involved have been relatively small. Soviet officials have also toned down allegations that US suppliers are unreliable. This shift in Soviet attitude combined with the continued Soviet belief that US technology and equipment

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are superior will put US firms in an improved position to compete against foreign firms. [REDACTED]

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Soviet traders have shown particular interest in US petroleum equipment such as electric submersible oil pumps, oil-refining technology and equipment, a plant for sour gas processing, and a facility to manufacture subsea oil and gas production equipment. In addition, Western firms bidding as prime contractors for major field development projects are soliciting US suppliers as subcontractors. Gorbachev's role in the Soviet agricultural sector in recent years may spur Soviet efforts to obtain Western technology for this sector and the large US agribusiness sector probably will give US firms an advantage over other Western firms. [REDACTED]

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[REDACTED]

Despite these increased opportunities for US business, the US is not likely to regain the position it held in the early 1970's. Events over the last ten years have eroded US competitiveness. Moscow has since developed and deepened its ties with non-US firms and Soviet concern over the reliability of US suppliers will take a long time to dispel. In addition, the hard currency stringencies which we anticipate that Moscow will face at least through 1990 will constrain the size of the pie which the US must share with Moscow's other hard currency trading partners.<sup>3</sup> [REDACTED]

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## Appendix B

### Attitudes of Western Governments Toward Trade with the USSR

#### West Germany

Bonn is currently not overly concerned about its trade deficit with the USSR and is not applying pressure on Moscow to end the imbalance. The West German trade deficit increased from \$954 million in 1983 to \$1.4 billion last year.<sup>4</sup> Bonn continues to run a comfortable global trade surplus. [REDACTED]

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West Germany has not initiated any projects or set up any special credit facilities to boost exports to the USSR. Officially-backed export credits are available to the USSR and to other countries with good credit ratings. During a January 1985 meeting of the Soviet-German Joint Economic Commission in Bonn, West German participation in development projects during the 12th FYP was discussed. The West Germans expect, as in the past Soviet plans, to capture a large portion of the Soviet contracts. [REDACTED]

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Bonn may focus more on its trade imbalance with the USSR if the deficit becomes structural. Gas deliveries over the next decade will rise about 25% in volume, while West German exports associated with pipeline development are winding down. If its

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<sup>4</sup> This memorandum uses Soviet official trade statistics only. Soviet data can differ substantially from Western statistics. For example, West German trade data show that the trade balance shifted from a \$240 million surplus in 1983 to a \$750 million deficit in 1984. Much of the large discrepancies can be explained by differences in reporting of oil trade.

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global trade surplus is reduced by a future decline in the US  
dollar, Bonn might begin to actively pressure Moscow to buy more  
West German products. [REDACTED]

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France

In contrast, France has complained the most to the Soviets over its continuing trade deficit. Although France recorded a trade surplus with the USSR through 1978, after the second oil shock the trade balance has been consistently in the red. The deficit peaked at \$1.4 billion in 1982 and exceeded \$800 million last year. Energy imports, which account for over 85% of French imports from the Soviet Union, increased by 10 percent in 1984 as deliveries from the Siberian pipeline project began; gas imports are scheduled to increase again this year. On the export side, almost one-half of all French sales to the USSR are agricultural goods, while semi-manufactured goods and finished manufactured goods each account for about another 25 percent. [REDACTED]

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France and the USSR signed an agreement in early 1984 that committed the Soviets to move toward balancing trade by increasing their purchases from the French. Nonetheless, exports to the USSR in 1984 fell in volume terms. From the French perspective, the most disturbing trend in Franco-Soviet trade is the Soviet failure to place orders for capital equipment. Orders have fallen from over \$1.5 billion in 1981 to less than \$120 million last year--the lowest level since the late 1960s. [REDACTED]

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Until recently, the French had done little more than verbally protest over the deficit problem. In the last several weeks, however, they have adopted a more active approach. Renault has cancelled a deal to build an automobile plant, stating publicly that the Soviets had placed most of their

equipment orders with West German firms, rather than with Renault or other French companies. In addition, press stories before the early April meeting of the Franco-Soviet Large Commission meeting suggested that France would reduce purchases of natural gas if Moscow did not increase imports of French capital equipment. [REDACTED]

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[REDACTED]

At the same time, the French will continue to actively court the Soviets as customers. Paris is currently trying to get the Soviets to accept credits in European Currency Units in order to offer lower interest rates and compete more effectively with the FRG. After the early April meeting, Foreign Trade Minister Cresson said she wanted to wipe out the bilateral deficit this year and expected contracts for French gas equipment worth over \$400 million to be signed soon. [REDACTED]

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United Kingdom

Britain does not view its trade deficit with the USSR as a serious problem. The deficit with the Soviets grew from \$216 million in 1970 to \$430 million in 1979. After enjoying a surplus in 1980 and 1981, Britain's trade reverted to a deficit in 1982 which was \$750 million last year, down slightly from 1983. [REDACTED]

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Despite their relative lack of concern, the British are attempting to increase exports to the USSR. London and Moscow recently have resumed trade talks curtailed following the Soviet invasion of Afghanistan. British companies hope to land major contracts to sell petrochemical, chemical, and biotechnology processes to the Soviets this year. In his December visit to London, General Secretary Gorbachev said he saw "good opportunities" for British companies in the areas of machinery, agriculture, food processing, and chemicals in the Soviet Union. [REDACTED]

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In the past, the UK has been willing to offer attractive credit terms to promote exports to the USSR and we believe London will continue using exports credits to increase trade in the future. In 1983, for example, the government Export Credits Guarantee Department (ECGD) offered a Soviet company financing for the purchase of oil field equipment at 7.5 percent, well below the market rate. Such terms represent a common practice of the ECGD and are not unique to trade with the Soviets. [REDACTED]

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Italy

Like the French, the Italians have been greatly disturbed by the size of the Soviet trade surplus, although they have yet to take strong measures to deal with the problem. The trade imbalance with the USSR has been increasing steadily since 1974. The deficit climbed over the billion-dollar plateau in 1980, and last year's deficit reached a record \$2.3 billion.

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Because of the lack of progress in reducing the trade imbalance, Italian officials considered cutting back on fuel purchases during 1984, according to the US Embassy in Rome. More recently, however, they appear to have shelved this option because Italy faces a possible protracted renegotiation of its gas contract with Algeria that may make Soviet supplies more necessary.

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In this regard, the Siberian gas accord, pushed strongly by the Italian business community, was accompanied by a commercial agreement committing the Soviets to cut the \$2.1 billion 1983 deficit in half by 1986 and to spend the income from the new gas contract on Italian goods and services. The Soviet commitment was made, however, with the stipulation that Italian goods be competitive both in price and financing. A multitude of cooperation and collaboration agreements followed in almost every industrial field but, despite initial business euphoria over the prospects of stepped up sales, actual contract signings have not lived up to expectations.

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Nonetheless, Italian officials remain optimistic that they are on the verge of expanding exports to the Soviet Union and cutting back the trade deficit. Numerous small contracts were signed in 1984, and two fairly large contracts have been concluded this year. One contract, a joint venture between an Austrian and an Italian firm, is for producing steel cord for radial tires. The contract is valued at \$220 million for the Italian firm Danieli, which absorbed one point to lower the financing cost to 7.5 percent over five years. The Italian company Cogolo will construct three shoe factories in the USSR for a total of \$60 million. [REDACTED]

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Italian officials also report that negotiations are underway for about \$5 billion in additional contracts. Several contracts are reportedly ready to be signed, including the construction of a one million metric ton-a-year turnkey steel plant at Volgograd valued at about \$1 billion, a \$200-million oil-drilling-pipe plant, a \$750 million coal slurry pipeline project in Novosibirsk, and up to \$750 million in contracts for automotive and agricultural equipment. [REDACTED]

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Italian companies also hope to conclude contracts for turnkey textile, chemical, and agroindustrial projects. IRI, the Italian state holding company, expects to participate in Soviet plans to modernize its steel industry, and the Soviets have expressed interest in Italian technology for flexible manufacturing equipment, automated assembly lines and gas injection equipment to increase output from aging oil fields. [REDACTED]

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Japan

Since 1982, trade between Japan and the Soviet Union has fallen sharply. Following a 20 percent drop from 1982 to 1983, two-way trade in 1984 declined another 12 percent to \$3.6 billion, with a Japanese surplus of \$1.5 million. The Soviet share of Japan's 1984 global trade was only 1.5 percent of exports and 1.0 percent of imports. [REDACTED]

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Japan has traditionally imported primary products from the USSR, but Japanese demand for Soviet goods has not been boosted by the recovery of the Japanese economy. Japanese interest in Soviet energy projects is based principally on the desire to sell equipment rather than to purchase coal, oil, or natural gas.

On the other hand, Soviet efforts to expand exports, especially of non-energy items has led Moscow to push strongly for counterpurchase or barter trade, which the Japanese have rejected. In addition, Tokyo has refused Soviet requests for a major reduction in the interest rates charged by the Japanese on deferred payments for imports. Japan's own policies to support US moves to check Soviet initiatives, moreover, have discouraged expanded trade relations. The net effect of Tokyo's behavior has been to shelve official trade and economic contacts with the Soviets. As recent changes in US-Soviet relations and in Soviet leadership have emerged, both Prime Minister Nakasone and Foreign Minister Abe have made smoothing relations with Moscow a priority. In fact, the resumption of political and economic exchanges since mid-1984 has been viewed in Japan and elsewhere as a thaw in relations between Tokyo and Moscow. [REDACTED]

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Japanese industrial leaders--especially in the trading companies--anticipate that the expanding bilateral dialogue, Gorbachev's rise to power, and the preparations under way for a new Soviet five year plan will bring increased trade. We believe, however, that Japanese industry, although willing to discuss new development projects, will be slow to make commitments. Ongoing joint resource development ventures are progressing slowly, if at all. Japanese equipment manufacturers are interested in sales to the Soviet Union, which such projects promote, but problems in developing the Siberian infrastructure and continued low demand for Siberian resources will continue to discourage a larger Japanese role in Siberian joint development. [REDACTED]

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